RECENT EVALUATIONS OF A.I.D. COMMODITY IMPORT PROGRAMS (CIPs)

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In l984 PPC/CDIE launched an effort to develop guidelines for evaluating non-project assistance {1}. In addition, during l984 there were 4 CIP evaluations:

- o Zimbabwe CIP, evaluated February l984.
- o Somalia CIP I and II, evaluated April l984.
- o Egypt public sector CIP, evaluated December l984.
- o Egypt private sector Production Credit Project-CIP (PCP-CIP), evaluated December l984.

While these evaluations do not cover all A.I.D. CIPs, they do provide a good cross-section of the various types of CIPs. They also demonstrate the possible roles policy reform, beneficiary targeting, foreign exchange rates and local currency programming can play in a program. This paper is designed to point out the different ways those CIP issues have been treated and some common "Lessons-Learned". It also offers some suggestions on how to deal with these issues when designing future CIP programs.

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1 Suggested Evaluation Guidelines for Non-Project Assistance, Prepared by Development Associates, Inc., October, l984

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1. SUMMARY {2}

While most of A.I.D.'s development efforts are project oriented, non-project assistance (CIPs and cash transfers) have been a substantial part of A.I.D.'s portfolio. In l966-l982 non-project assistance represented roughly 37 percent of A.I.D.'s program; in recent years it has been over 40 percent of the program. Looking at the components of non-project assistance, the case is somewhat different. The CIP share has been declining while cash transfers have increased sharply.

A CIP is essentially a tied foreign exchange program designed for fast disbursement, to help an LDC meet a foreign exchange shortfall. A CIP allows an LDC to import a wide range of goods from the U.S. and in some cases, from selected LDCs. In contrast, a cash transfer represents free foreign exchange. An LDC can use a cash transfer for any purpose since it is not tied to purchases in the U.S.

CIPs are usually designed to support LDC policy reforms. However, the evaluations found the CIP-policy linkage weak. In Egypt both the public and private sector CIPs lacked policy conditionality. (In fact, a perverse GOE interest rate structure and other policies prevented the Production Credit Project-CIP (PCP-CIP) from encouraging medium-term private sector investment.) In Zimbabwe the CIP also lacked policy conditions. On the other hand, in Somalia there were a number of policy conditions and the host government did initiate a package of reforms. The linkage of the A.I.D. CIP to the Somali IMF Agreement did create problems when Somalia was unable to stay in compliance with the Fund.

Each Mission has a CDSS which lays-out its program strategy. Ideally, all A.I.D. inputs should support that strategy. That can be difficult with CIPs. If a CIP is to support a strategy based on small-farmer welfare, increased agricultural production and employment, then the CIP commodities need to be carefully selected and targeted to reach specific beneciaries. However, such targeting could turn the CIP into a project. It would require detailed commodity and beneficiary analysis along with supporting technical assistance. While Missions did some commodity screening, procurement was generally open to all Reg. 1 commodities. The evaluations found some cases where CIP commodities did not fit CDSS objectives. Faced with a trade-off between targeting and rapid disbursements, CIPs generally were designed to meet the disbursement objective.

Related to the targeting issue was the issue of foreign exchange rates and subsidies. Each evaluation found that CIP imports were offered to LDC importers at the "official" exchange rate. That rate was 30-100 percent below the free market rate. While the importer faced other costs in using the CIP, there still was a major opportunity for a windfall profit. On the other hand, the evaluations found that for most LDC importers, a CIP was not as desirable as free foreign exchange. Tying CIP procurement to A.I.D. rules and U.S. source could make CIP commodities more expensive. In Egypt, a foreign exchange subsidy was needed to move CIP commodities.

The final area was local currency programming. In Egypt, A.I.D. involvement was minimal. In Zimbabwe AID was heavily involved and used the local currency as a major development tool. The Zimbabwe case shows that A.I.D. can use counterpart funds creatively to affect host government budget allocations and sectoral priorities.

Based on these evaluation findings, there are a number of policy approaches which could strengthen the economic impact of CIPs. These should be considered when designing future programs:

- Policy Reform

Policy dialogue and policy reform are central to most CIPs. However, CIP policy goals are often hard to specifically pin down. Thus, it is difficult to monitor the policy impact of most CIPs. If a "policy checklist" was included in the original project paper it could serve as a useful tool for Mission management.

- Targeting -- Commodities and Beneficiaries

There is a natural programming tension in any CIP between rapid disbursement rates and targeting commodities to CDSS designated beneficiaries. The CIPs reviewed in this paper chose to emphasize disbursement rates. In future CIPs it might make sense to more tightly limit commodity eligibility and importers to those that are most directly linked to A.I.D.'s CDSS strategy.

- Foreign Exchange Rates

When designing a CIP, A.I.D. should critically examine the spread between the official and free market exchange rates. If the difference is large, A.I.D. should consider including policy conditions to narrow the spread. Alternatively, A.I.D. should consider providing the CIP at a rate closer to the free market rate.

- Local Currency Programming

A more activist approach to programming CIP local currency provides an opportunity to direct a portion of an LDC's domestic resources into areas which fit A.I.D.'s developmental strategy. As demonstrated in the Zimbabwe CIP, A.I.D. can have a key impact on an LDC's development budget priorities. The extra management costs of such an approach should be carefully weighed against the opportunity for increased developmental impact.

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2 This paper is designed to look at CIPs and therefore only examines A.I.D., Foreign Assistance Act resources. PL 480, a form of non-project assistance, is not included.

2. NON-PROJECT ASSISTANCE, CHANGING ROLES FOR CIPs AND CASH TRANSFERS

A.I.D. provides both project and non-project assistance. Project assistance is defined as a single activity, that uses a number of inputs to generate specific and discrete outputs. For example, a rural education project designed to raise literacy rates might include aid funding for teacher training centers, curriculum development, participant training, advisors and school construction. Non-project assistance is much broader in scope.

Non-project assistance is used to support LDC policy reform, economic stabilization and sectoral programs. Since the objectives deal with broad economic and policy issues it is not necessary to link assistance disbursements to actual physical outputs such as building schools.

There are two ways of providing non-project assistance. A cash transfer, as the name implies, is the transfer of money directly to an LDC. Funds from a cash transfer can generally be used by the LDC for any imports, from any source it chooses.

A C.I.P. is more restrictive. C.I.P. funds can be used to purchase designated commodities from the U.S. and in some cases, from selected LDCs. A.I.D. rules on source/orgin, competitive bidding, "fair prices", 50/50 shipping and other requirements apply to C.I.P.s. In contrast, a cash transfer represent free foreign exchange which an LDC can use for any purpose it chooses.

Commodity Import Programs (CIPs) go back in time to the Marshall Plan. In fact, the basic CIP procedural document, Regulation 1, was originally issued in l948 and has been regularly updated ever since. CIPs have been used throughout the history of U.S. economic assistance and until recently, have represented a major part of A.I.D.'s program. In recent years CIPs have fallen sharply as cash transfers have gained increased importance.

Excluding PL 480{3} and dealing with only A.I.D. Foreign Assistance Act resources, non-project assistance has grown in absolute amount and as a share of the total A.I.D. program (see Table 1). CIPs and cash transfers were roughly 37 percent of A.I.D.'s program during l966 to l982. They increased slightly in the last two years to 42 percent in l983 and 43 percent in l984.

Within non-project assistance there has been a major shift to cash transfers. During FY l966-l970 cash transfers of $25 million a year represented 1 percent of A.I.D.'s program. In FY l983 and l984 cash transfers had increased to $1.6 billion and represented one-third of A.I.D.'s total program (see table 1). During the same period CIPs declined in both absolute and relative terms. In FYs l966-70 CIPs of $842 million a year were 38 percent of A.I.D.'s program. In l983 and l984 they averaged $532 million a year and represented only 10 percent of the program. There has been a major structural change within nonproject assistance as CIPs have declined and cash grants have increased sharply. There has also been a parallel change as political/security concerns have assumed more importance in non-project assistance programs.

In the period l966-l974 only about 40 percent of CIP programs were financed out of Security Supporting Assistance and the remaining 60 percent were financed from development accounts. Nearly all CIPs were designed to support broad developmental objectives and policy reforms dealing with foreign exchange rates, import liberalization, industrial policy and food policy. CIPs were centered on countries like India, Pakistan, Colombia, and Korea that were undertaking economy-wide structural adjustments. However, starting in the mid-l970s there was a change in non-project emphasis with a switch to cash transfers and an increased emphasis on a political/security justification.

Since l975 all CIPs have been financed from ESF (or the previous Security Supporting Assistance) and none from Development Assistance. While CIP programs still are targeted on balance of payments or budgetary problems, the predominent justification is now political, not macro-economic.

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3 Some 53 percent of the FY l984 PL 480 budget was non-project assistance (Titles I and III). The non-project portion of the FY l984 A.I.D. budget was 43 percent. Combining the A.I.D. and PL 480 budgets, non-project assistance was 45 percent of the total.

3. POLICY CONSIDERATIONS

A shortage of foreign exchange can be a serious impediment to economic/political stability and economic growth. In such a case, generalized short-term foreign exchange support may be the most effective way of contributing to stabilization and economic growth.

CIPs are usually justified, on the need to close a foreign exchange gap, i.e. CIP resources will allow a higher level of GNP growth. However, compared to a CIP, a drought or changes in the prices of export crops can have a much greater balance of payments impact. Given these large external factors and the relatively small size of most CIPs, it is difficult to demonstrate a direct CIP/GNP growth rate linkage. The Egypt and Zimbabwe evaluations were only able to make very rough estimates of CIP generated output and employment benefits.

Still, a CIP's major selling point is its ability to provide rapid disbursements to fill a short-term balance of payments need. If an LDC has idle capacity, then a CIP can provide raw materials and spares which should rapidly boost output. The key point is whether the LDC has the programs, policies and market incentives in place to effectively use the additional resources.

Nearly every LDC could use more foreign exchange. However, balance of payments considerations are not in themselves a sufficient basis for a CIP. If a CIP is provided for primarily economic rather than political reasons, a concrete link between the assistance and sound economic policies needs to be demonstrated. Foreign exchange gaps are often traced to inappropriate economic policies, the reform of which is essential to any assistance effort. In that sense CIPs buy time. If that time allows the introduction of corrective policies and structural changes, the CIP money is well spent. Thus, the key component of any CIP is the identification of structural problems and the needed policy reforms that will put the economy back on the path to sustained development.

The Somalia CIP I and II were designed to provide a foreign exchange injection of urgently needed equipment and spare parts. The CIPs were successful in providing such imports in a timely fashion. They were also designed to support policy reforms that included a reduction in government administrative controls, a greater reliance on market forces and the encouragement of the private sector. The CIP policy reforms were tied in part to policy reforms to be undertaken through an IMF agreement.

While it is hard to identify causality, a number of policy reforms did take place during the period when the Somalia CIPs were in effect. However, the evaluation found a problem with linking CIP performance to an IMF program. While there is always the question of whether IMF conditions match A.I.D. concerns, in the case of CIP II, Somalia and the Fund were unable to negotiate an agreement. But, the CIP had a condition requiring Somalia to implement an agreement with the IMF. This created a problem for A.I.D.. In effect the CIP had become an accessory to the IMF Agreement.

Policy reform is always difficult to negotiate. Riding the IMF's policy coat-tails may appear to be a solution. However, the Somali case shows that tying A.I.D. policy reforms to an IMF agreement is not an easy solution. A.I.D. needs to identify the policy changes that are needed and then use the CIP itself to achieve those reforms. If they can be linked to the IMF program, so much the better. But, A.I.D. cannot turn over its policy proxy to the IMF.

The first Zimbabwe CIP was part of the U.S. assistance package promised to newly independent Zimbabwe. While it was provided for predominently political reasons (to help assure a peaceful transition from war-torn Southern Rhodesia to an independent Zimbabwe), post-war reconstruction and the resumption of economic growth made those political objectives possible.

The CIP provided capital goods, spares and raw materials to support industrial growth. The CIP disbursed rapidly and generated significant increases in industrial output and employment.

The Zimbabwe CIP lacked macro-economic policy conditions. There was no macro policy conditionality or macro policy reform effort. However, the CIP is a good example of the way sectoral policy changes can be achieved through local currency programing. Its impact on the Zimbabwe Government's sectoral investment priorities was a major program success (see Section VI below).

Over a period of 10 years, A.I.D. has provided the Egyptian public sector with a series of annual CIPs. The CIPs were designed to ease Egypt's balance of payments pressures, as part of the Egypt/Israel peace effort. CIPs in recent years have been provided on a grant basis, at roughly $300 million a year for use by the public sector. The CIPs eased balance of payments pressures and provided imported U.S. commodities vital to the operation of a number of government ministries and parastals.

The evaluation was unable to find any CIP policy impact. That is understandable since the CIP was not designed around specific policy problems or policy reforms. While the CIP itself was not linked to specific performance criteria, it was one element in the Mission's total assistance package which did form the basis for policy discussions with the Egyptian Government.

The Egypt private sector CIP (PCP-CIP) was somewhat different from the public sector CIP. It was designed more like a project and was expected to do more than most CIPs -- to provide U.S. imports, short and medium term credit to the Egyptian private sector and technical assistance to improve Egypt's financial markets. The PCP-CIP was able to achieve its CIP objectives of providing U.S. imports to the private sector. It was not able to achieve its broader aim of encouraging more Egyptian private sector investment.

The Central Bank of Egypt had set a maximum interest rate of 13 percent on longer-term industrial credit and a 16-18 percent minimum on short-term trade credits. These rates were designed to encourage longer-term productive investment while discouraging short-term, commercial loans. In fact, they had the opposite effect. The banks saw where the profit was and put the bulk of the money into short-term commercial loans. In addition, Egyptian importers were fearful of a devaluation. PCP loans were effectively tied to the foreign exchange rate in effect when a loan was repaid. Importers were reluctant to take the foreign exchange risk of borrowing under the PCP program.

The PCP-CIP was a good example of a case where the provision of more financial resources (foreign exchange and local currency) could not solve structural misallocations caused by inappropriate policies. The evaluation found that such policy issues could not be resolved in the context of a single, relatively small project. It requires macro policy changes dealt with at a much higher level. The project was able to move foreign exchange but, in the absence of policy reforms, it did little to change the factors that were restricting private investment.

4. TARGETING -- COMMODITIES AND BENEFICIARIES

In any CIP there is the question of the degree to which CIP commodities should be specified and targeted to support A.I.D.'s development strategy. In most countries this would mean targeting commodities to benefit the rural poor and concentrating on efficent industries serving A.I.D.'s target beneficiaries. However, if import categories are limited and directed to specific beneficiaries, disbursement rates may suffer. The evaluations found that all of the CIPs had to deal with this problem. In large measure, they stayed away from targeting in order to encourage rapid disbursements.

The Egypt CIPs were much like the CIPs in Zimbabwe and Somalia; funding in Egypt was directed to a large number of areas:

- raw materials and foodstuffs
- capital goods and spares
- producers of foodstuffs, agricultural supplies, and irrigation
- industry, including government parastatals
- producers of services including transportation, and tourism
  communications, housing construction, utilities, roads and tourism
- production societies including cooperatives and private hospitals
- private entrepreneurs such as doctors, engineers, accountants and agriculturalists
- small equipment and intermediate goods for use in industry, transport, health and education

Since the eligible categories were broad, there were bound to be some imports that would not directly match the Mission's CDSS strategy. For example, A.I.D.'s Egypt health strategy emphasized low-cost rural health care. However, the private sector CIP funded sophisticated diagnostic and treatment equipment for private sector doctors. On the agriculture side the PCP-CIP funded crop spraying aircraft for use on large irrigated farms. This was not directly related to A.I.D.'s normal small- farmer approach.

In Zimbabwe, large farmers imported large, high horsepower tractors and harvesters. In a country where the CDSS has an employment strategy and stresses small farmer development, sophisticated capital equipment for large farmers could be questioned. The CIP also financed $6.3 million of computers and data processing equipment -- a transaction that would have been difficult to include as a development project in Zimbabwe's rural and employment-based ABS.

5. CIP FOREIGN EXCHANGE RATE

An important concern is whether importers who gained access to CIPs were making windfall profits. In Somalia the CIP was available at the "official" foreign exchange rate. The "free" market rate was 60-100 percent above the official rate. In Egypt the "free" market rate was 30-40 percent above the official rate. In Zimbabwe there was a similar divergence between the official and free market rates.

In all three countries foreign exchange was administratively rationed and the official rate was well below the free market rate. Importers who were able to claim a piece of the CIP were probably able to make an extra profit. That had, in fact, been a concern with earlier private sector CIPs in Egypt. Traders would import commodities, sell them to end-users and turn a quick profit. To avoid such a problem the PCP-CIP tried to limit trader access.

While there is always the danger that CIP goods may be priced too cheaply, the opposite can also happen. If CIP goods are too expensive, LDC importers will be reluctant to use the CIP and CIP disbursement rates will suffer. To LDC importers a CIP, like any tied aid, is not as valuable as free foreign exchange. An LDC importer also has to deal with 50/50 shipping and other A.I.D. rules which raise the effective cost of AID CIP commodities. In addition, with the recent strength in the U.S. dollar, many U.S. commodities are priced much higher than similar goods sourced from Europe or Japan. The Egypt PCP-CIP evaluation compared the cost of similar goods imported from the U.S. under A.I.D. financing to free foreign exchange imports from Europe. It found that during l983 (before the major rise in the value of the U.S. dollar) an Egyptian importer had to pay 20-30 percent more for A.I.D. goods. If both European and CIP funds are offered at the same foreign exchange rate, the importer would naturally opt for the cheaper European goods. In such a case, if a tied CIP is to disburse, it would need a foreign exchange rate 20-30 percent better then European funds. There was a 20-30 percent differential between the official and free market rates during the early years of PCP-CIP disbursements. In latter years the differential widened to over 40 percent and windfall profits were possible.

CIPs are provided to meet an immediate balance of payments need and A.I.D. is interested in rapid disbursement rates. In a case like Egypt, if the CIP recipient has other foreign exchange resources, the CIP must be priced at a rate that moves the U.S. goods. If a large foreign exchange rate subsidy is required then there is the question of whether this is the most effective way to use U.S. funds. Project assistance, technical assistance or even a cash transfer might make more sense.

The Egypt case may be unique. The Egypt PCP-CIP evaluation covered l983 and early l984 when Egyptian free foreign exchange and aid from non-U.S. sources was relatively plentiful. The Zimbabwe and Somalia CIPs may be more typical usual A.I.D. recipient. In Zimbabwe and Somalia the evaluations found that foreign exchange was so scarce importers were willing to pay the higher cost for U.S. source goods.

In the more normal LDC situation of foreign exchange scarcity, A.I.D. needs to be concerned with the effects of an overvalued foreign exchange rate. The LDC may import inappropriate commodities that do not reflect the economy's "real needs", e.g. imported commodities that fail to reflect the LDC's labor/ capital ratio. In addition, CIP importers may make windfall profits from CIP imports that are available at the "cheap", official exchange rate. In such cases A.I.D. needs to work with the LDC, the IMF, World Bank and other donors to move the rate closer to the true scarcity value of foreign exchange.

6. LOCAL CURRENCY PROGRAMMING

A CIP is designed to ease balance of payments pressures. The real resource transfer takes place when imported CIP goods are provided to an LDC.

In strict economic terms the imported commodities are the additive resource to the economy. Local currency counterpart is generated but does not represent an additive, real resource to the LDC.{4} Still, whether the local currency is an additive resource or not it is generated and A.I.D. can participate in decisions on its allocations/uses. The four CIPs demonstrated the various degrees of possible A.I.D. involvement in local currency programming.

The Egypt public and private sector CIPs are examples of minimal A.I.D. involvement in the programming process. The evaluation found that the GOE " ... credited such funds to A.I.D. projects, but there was no USA.I.D. involvement in those decisions. USA.I.D. policy appears to be close to a "laissez-faire" position." The evaluation concluded that "thus far the Special Account funds have made no measurable developmental impact."

In Somalia, CIP generated local currency was programmed for development projects by a joint A.I.D./Ministry of Finance Committee. At the time of the evaluation only limited counterpart generations had been programmed. Local currency had been allocated to A.I.D.'s Kismayo Port Project and to the Somali Development Bank for medium-term agricultural and agro-industrial loans.

The Zimbabwe CIP had the most activist approach. A.I.D. Mission technical offices worked closely with their counterparts to identify specific investment projects in the education, health and agricultural sectors. The Mission and the Ministry of Finance then agreed on specific projects that would be funded. The A.I.D. Mission closely monitored the construction and operation of those projects. At a time when Zimbabwe was sharply cutting back on its development budget, A.I.D. was able to assure funding of those projects it had identified as most critical. In a sense A.I.D. was intervening in the host government's budget process to promote key projects and sectors. The Mission considered the local currency programming as important, if not more important, than the CIP commodities.

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4 An illustrative example might help explain the additionality issue . If an LDC's domestic economy is producing $1000 and A.I.D. provides a CIP of $10, then the economy has a total resource availability of $1010. If the A.I.D. CIP generates local currency of $10, that is not an additive resource. The economy does not have resources of $1020. It only has $1010. But, if A.I.D. programs the local currency it does have a say in how those 10 units of local resources are used. In that sense the CIP does doubleduty. A.I.D. decides what types of additive imported commodities will be made available to the economy and A.I.D. also has a say in the allocation of an equivalent amount of local resources.

Table 1

A.I.D. CIPs, Cash Transfers and Other Financing
FYs 1966 to 1984
($ millions)

	Time Periods				
	l966-70 Annual Average	l971-78 Annual Average	l979-82 Annuual Average	l983	l984
DOLLAR AMOUNTS					
CIPs	842	721	437	502	563
Cash Transfer	25	240	1089	1590	1697
Other Financing	1332	1699	2558	2840	3030
Total	2199	2660	4084	4932	5290
PERCENTAGE SHARES					
CIP Share of Total	38%	27%	10%	10%	11%

Cash Share of Total	1%	9%	26%	32%	32%
CIP and Cash Share of Total	39%	36%	37%	42%	43%

Data Sources:
FY l966-1982; D. Brown Oct. l982 Report, CIPs as a Development Tool
FY l983, l984; PPC/PB/PIA
Note: Includes A.I.D. Foreign Assistance Act Resources. Does not include PL 480.

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Table 2

CIP Regional Obligations Trends
FY l966 to 1984
($ millions)

	1966-70 Annual Average	1971-78 Annual Average	1979-82 Annual Average	1983	1984
Latin America	209	1	0	0	0
Africa	24	18	87	142	170
Asia	398	106	15	60	92
Vietnam	138	162	-	-	-
Near East	73	434	335	300	301
TOTAL	842	721	437	502	563

Data Sources:

FY l966-1982; D. Brown Oct. l982 Report, CIPs as a
Development Tool
FY l983, l984; PPC/PB/PIA

Note: Includes A.I.D. Foreign Assistance Act Resources. Does not include PL 480.

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Table 3

A.I.D. Commodity Import Programs (CIPs)
($ millions)

	FY l983	FY l984
Africa	142.250	170.000
Zambia	15.000	15.000
Zimbabwe	37.000	10.000
Kenya	--	21.000
Mauritius	2.000	4.000
Somalia	16.000	--
Sudan	60,250	102.000
Mozambique	--	6.000
Zaire	--	10.000
Seychelles	2.000	2.000
Niger	5.000	--
Senegal	5.000	--
Near East	300.000	301.055
Egypt	300.000	301.055
Asia	60.000	92.000
Pakistan	60.000	92.000

TOTAL	502.250	563.055

Data Source: PPC/PB/PIA
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